national farmers union

In Union Is Strength

...UE SOUTH
...SK. S7K 2M1
...) 652-9465

National Farmers Union

Submission

to the

Standing Committee
on
Finance, Trade and Economic Affairs

presented

..., Ontario

March 20, 1985

250C - 2ND AVENUE SOUTH
SASKATOON, SASK. S7K 2M1
TELEPHONE (306) 652-9465

national farmers union

In Union Is Strength

National Farmers Union

Submission

to the

Standing Committee
on
Finance, Trade and Economic Affairs

presented

Ottawa, Ontario March 20, 1985

National Farmers Union

Submission

to the

Standing Committee

on

Finance, Trade and Economic Affairs

presented

Ottawa, Ontario March 20, 1985

INTRODUCTION:

We welcome the opportunity of discussing with your Committee the three issues under review related to farm finance and taxation.

As a direct membership organization of farm families, our members are among those directly affected by government policies related to these matters.

Members of the Committee should know that our organization has since its inception in 1969, offered income tax filing and business accounting services for members where sufficient numbers have indicated the need for such services exist. We can additionally report that prior to provincial farm unions becoming part of the NFU, such services were in existence dating back to the early 1950's in Saskatchewan and Manitoba.

The objective of providing these services at cost, aside from fulfilling their basic responsibility as good citizens, has always been based on our recognition of the importance for farmers to develop better understanding of the business end of farming. Perhaps that has heightened awareness among our members that the economics of farming are somewhat less than they themselves may have realized and basic farm policy changes by governments are often indicated.

Our relationships with Revenue Canada at the various places we have contact with them has always been first class in dealing with the affairs of our client members.

FARM INCOME - A BASIC POLICY ISSUE:

It is appropriate to observe that if farmers were to receive prices for their products which properly reflected average costs of production and a reasonable return for investment capital, labour and management, it would be unnecessary to discuss the three issues under review.

If farmers, for example, did not in large measure need to rely upon the equity value of their farms as a potential retirement fund but could provide for their retirement funding on an annual basis out of earned income, as do professionals, many wage and salary earners (including civil servants and M.P.s), the issue of capital gains on the sale of farms could be routinely handled in accordance with standard public policy.

Similarly, Section 31 would not be a consideration. Surplus earnings on the sale of farm produce could constitute the primary source of reinvestment funding for combined income farmers and any additional investment from off-farm sources would only hasten the day for their establishment as full-time operators, should that be their objective.

Farmers would not need to seek special preference in farm credit funding if an administered food pricing system were in effect instead of the current chaotic and unrelated pricing structure that controls most of our farm production.

It is the steadfast adherence of government policy to the principle that the free market pricing system is the best allocator of resources that has given rise to many of the problems evident in farming today.

The popular myth that administered pricing for farm products costs the consumer more, by inference implies that consumers are entitled to and deserve cheap food. As we know, farmers do not control the open market pricing of farm products. They are price takers. For

them to influence open market price changes requires rearrangement of power sharing by the processing and manufacturing sectors. It further requires more orderly marketing and management of supply which also contributes toward stability of supply.

That such an arrangement might not cost the consumer more was graphically illustrated in the winter 1984/85 edition of "Egg Update", a publication of the Canadian Egg Marketing Agency and appears as Appendix A.

Essentially then, in the discussion of the three issues before us, we are once again dealing with symptoms rather than with the basic causes of inadequate farm income, and that fact is a matter of regret to us.

As a consequence, the agricultural industry continues to remain one of contradiction and contrast. On the one hand we have highly productive sectors that lend credibility to our claim of being highly efficient and viable. Approximately one-quarter of our farms now account for three-quarters of our food production.

On the other end of the spectrum are those who might not be capable of any longer generating adequate income at any price to earn a livelihood because their resources simply are inadequate.

In between are those who under proper policy could survive and contribute a great deal toward the economy and society. Included among this group are many beginning and medium sized operations which are in some cases surviving through the direct subsidization by off-farm income of the food they produce and indirect subsidization through free family labour and subsistence living standards.

It is an elementary equation in farming that: volume x price = income. The pull of policy is in the direction of the argument that if a farmer produces more, he can accept a lower price and still end up with an acceptable income, assuming he can survive the cost factor.

What essentially results is that rather than all of agriculture being proportionately rewarded by higher income as a result of greater productivity, the benefits of farm efficiency primarily accrue to the non-farm sector. While consumers have been nurtured in the belief that they too are major price benefactors of the free market system, the findings reported in Appendix A refute this.

Nationally, the index of farm production rose from 103.0 to 131.7 or by 28%, between 1975 and 1983, (1971 = 100). That most farmers are the victims of pricing policies that provide narrowing margins of return on growing volumes of production is evident when farm cash receipts are compared to realized net farm income in the ten year period, 1975 - 1984.

In current dollars, 1984 cash receipts doubled those of 1975 while realized net income remained exactly the same. In constant dollar value, 1984 realized net income had one-half the purchasing power of 1975 net income. (Appendix B)

Canada's national agricultural policy continues to be essentially based on a philosophy of attrition in farm numbers which is intended to encourage expansion of farm size and industrialization thereby resulting in farm depopulation.

AGRIBONDS:

During the course of the 1984 federal election campaign, the Progressive Conservative Party unveiled its policy program for agriculture at the Prince Albert Caucus convened on July 5.

The subject of Agribonds was included as item Number 3 in a 16-point program and stated as follows:

> "We will establish an Agribond Program to provide loans at reduced rates to producers. A tax exemption for earned income on these bonds will be provided to encourage people to invest in this program."

We assume that consideration for implementation of an Agribond

Program was prompted by the acknowledged high interest rates that continue to prevail in Canada, rising production costs and the stagnant prices for agricultural products which have made it difficult for many farmers to make ends meet.

The public media, following the release of Finance Minister Wilson's discussion paper on Taxation, widely portrayed the average farmer in Canada as being rich, having assets of over $508,000 and equity of $417,000. In so doing they performed a disservice to the country and an injustice to many farmers who desperately need to have the financial problems which confront them better understood by the non-farm sector. Equity is a paper figure and no absolute measurement for determining a farm's real wealth, earning ability or cash flow potential. Should sufficient numbers of farmers be forced or simply offer their equity for sale at any given time, the value of farm equity could simply collapse on an overburdened market. The call for lower interest rates is a partial response to prevent that from occurring and to maintain the health of the entire industry. That such a policy is required is not in dispute.

Government needs to assure that:

a) The maximum possible interest rate reduction available under any program must accrue to the farmer;

b) The administration of such an interest rate reduction program must be as efficient and simple as possible;

c) The recipients of such assistance must be targetted;

d) The cost of the program to the federal treasury must be predictable within a reasonable degree of accuracy and responsive to changing conditions.

The discussion paper indicates that a reduction in farm financing costs of 4 percentage points would impose direct costs of some $40 million for each $1 billion of agribond lending.

While a 4 percent reduction in interest rates would represent a substantial amount, we believe it is preferable to target the interest rate reduction to establish a ceiling on the cost of credit to the target group. This ceiling, we recommend, should be no greater than 8 percent.

In consideration of this proposal, we draw your attention to wide variation of lending rates of the Farm Credit Corporation since 1971 as indicated in the following tables:

Under the Farm Credit Act
En vertu de la Loi sur le crédit agricole

Effective date Date d'effet		Rate Taux	
01/04/71		7¾%	
01/10/71		7½%	
01/04/72		7%[1]	
01/10/72		7%[1]	(8%)
01/04/73		7%[1]	(7¾%)
01/10/73		7%[1]	(8½%)
01/04/74		8¼%	
01/10/74		9¼%[1]	(10%)
01/04/75		8½%	
01/10/75		9%	
01/04/76		9¾%	
01/10/76		10%	
01/04/77		9¼%	
01/10/77		9¼%	
01/04/78		9½%	
01/10/78		10%	
01/04/79		10¾%	
01/10/79		10¾%	
18/10/79		12%[1]	(10¾%)
01/04/80		13%	
01/10/80		12¾%	
01/04/81		14%	
01/10/81		16¾%	
01/04/82		16½%	
01/10/82		15¾%	
09/12/82		13¼%	
01/04/83		12¾%	
20/08/83		13½%	
01/10/83		13½%	
22/11/83		13%	
09/04/84[4]	- 5 yr. term	14%	
	- 10 yr. term	14 5/8%	
	- 20 yr. term	15%	

Under the Farm Syndicates Credit Act
En vertu de la Loi sur le crédit aux syndicats agricoles

Effective date Date d'effet	Rate[2] Taux	
01/04/71	7%	
01/10/71	6¾%[3]	
01/04/72	6¼%	
01/10/72	6¼%[3]	(7½%)
01/04/73	6¼%[3]	(7%)
01/10/73	6¼%[3]	(8¼%)
01/04/74	8%	
01/10/74	10%	
01/04/75	8%	
01/10/75	8¾%	
01/04/76	9½%	
01/10/76	9½%	
01/04/77	9%	
01/10/77	8¾%	
01/04/78	9%	
01/10/78	9¾%	
01/04/79	10¾%	
01/10/79	11%	
01/04/80	13¼%	
01/10/80	12¾%	
01/04/81	14%	
01/10/81	17½%	
01/04/82	16½%	
01/10/82	15¾%	
01/04/83	11½%	
01/10/83	12%	
24/04/84	13¾%	

Source: FCC/SCA

Reduction of interest rates to targetted borrowers to the 8 percent level would be more equitable to all than an across-the-board reduction where some would be perceived to benefit more than others. Such a program should be administered by the Farm Credit Corporation.

Our organization believes it is extremely important to retain

public involvement in farm lending programs. Farm credit programs essentially do not represent a cost to government but an investment in an industry that generates a great deal of wealth and benefit to the nation.

Public involvement in farm credit lending in Canada was originally necessitated in the 1940's by the total withdrawal by the private lending institutions in providing farm credit following the Great Depression. Following World War II, agriculture needed badly to be revitalized.

In recent years, government policies have encouraged agricultural lending by private lenders, however, it is apparent that this has not been universally satisfactory either from the standpoint of farmers or the lending institutions who have encountered the hazards of repayment that sometimes confront farmers.

While banks and credit unions have extended increasing amounts of credit to farmers, attaining over $11 billion in all outstanding credit in 1984, such lending has been extended on the assumption of full recovery. The farmer was the risk-taker in pricing, domestically and internationally, rising interest rates, natural disasters, etc. The concept of investment and risk sharing with the farmer is not one to which private lenders primarily subscribe.

We recommend that beginning farmers and farmers in financial distress receive priority as the target group of any interest rate reduction program, whether this be through direct subsidy or through an agribond program.

Should the Committee and the government elect to pursue the more complicated course of an investor-type Agribond program, we would nonetheless recommend that the principle of an 8 percent ceiling on interest rates to the target group be maintained.

In outlining the pros and cons of this program, the White Paper draws attention to the need for "controlling the scope of the program, the supply of funds by investors is particularly associated with the

tax-assisted agribond proposal".

We recommend that consideration be given to installing a ceiling on the investment which any single investor could make under the program in any year. This would regulate the inflow of funds and control the annual direct tax benefits which would accrue. Agribonds should additionally be government guaranteed in the same manner as Canada Savings Bonds but be non-redeemable for fixed terms, such as 5 or 10 years.

CAPITAL GAINS:

The P.C. July 5 policy position on capital gains in the sale of farm property states:

"We will abolish the imposition of capital gains tax on the sale of farm property for continued agricultural purposes."

Currently, tax provisions permit deferral of capital gains tax on farms transferred to children. Under this arrangement a farmer might gift his farm to a son and transfer future responsibility for full payment of any capital gains tax to him as part of the bargain. Alternately he may sell the farm for less than accepted market value and pay capital gains on the lesser amount. This would also establish an amended cost base on the farm for future taxation purposes.

While it may be argued that such an arrangement reflects a bias toward retaining a farm within the family, we believe it may also result in the rollover value of land sold to the son more accurately reflecting its productive value rather than its speculative market value. This fact alone would enable a son a better opportunity to retire any principle debt he may have incurred to satisfy the property transfer. From our standpoint, encouragement of a bias easing the potential burden of repayment on a beginning farmer is worthwhile.

The proposal for total abolition of capital gains tax on the sale of farm property if used for continued agricultural purposes somewhat distorts this general approach.

In the first instance, the sale of such property would not need to remain within the family. As a consequence, the market value of land would bear principle influence on the selling price.

Secondly, it is less likely such land would become available to a beginning farmer if he did not have a sufficiently large asset base to raise the required capital.

We believe it is important for farmers who purchase land to be able to claim interest costs as a charge against income for tax purposes. This concession on tax deferral in itself implies a future obligation toward the potential payment of capital gains.

We recommend the first $250,000 of capital gains on the sale of farm property be exempt from tax for any farmer who has farmed at least 10 years. As well, the current provisions permitting the rollover to an R.R.S.P. of $120,000 of taxable capital gains on the disposition of certain farm property should be allowed. This latter provision should be exclusive of any R.R.S.P. investments a farmer may have purchased in previous years.

SECTION 31:

Item 7 of the P.C. agriculture policy of July 5 stated as follows:

"We will change Section 31 of the Income Tax Act as it applies to farmers, to reflect the principles of equity, neutrality, simplicity and certainty. In addition, the strong-arm and confrontationist tactics presently practiced by the Department of Revenue will be immediately abolished and a practice whereby the taxpayer is treated openly and honestly will be instituted."

Of the three policy issues before this Committee, the issues surrounding Section 31 are probably the most difficult to resolve.

The discussion paper observes:

"The 1952 general provision prohibiting taxpayers from netting secondary business losses from their chief source of income was repealed. That opened the way for taxpayers to aggregate income and losses from all their activities and pay tax

only on the net amount. The only exceptions to this rule were taxpayers who incurred part-time farming losses."

It does not take a great deal of imagination to realize that if this type of discrimination had been directed toward other types of secondary business losses, the resulting chaos would have been at least as severe or more so than it is in farming.

It must additionally be obvious to the Committee that the $5,000 maximum deduction allowed in 1952 was a great deal more generous than it is in 1985.

Then Minister of Finance, Hon. Douglas Abbott defended the action by stating that ... "gentlemen farmers never make money from their farms. They always lose money; and they write off that loss against income from other sources, such as salary or investment income."

This is a prejudicial generalization and stereotype of persons who are now classed as part-time farmers which should be ended irrespective of their circumstances.

This attitude expresses an exaggeration of fact and is the source of inequity that calls for changes to the application of Section 31.

The discussion paper itself makes an additional judgment which creates a further problem confronting the progress of combined income farmers who wish to become better established in farming. It states on Page 25:

"There is also evidence that many part-time farmers self-restrict by restraining their use of tax incentives to keep their reported loss below the permissable limits. The restricted loss figure in Table 10 may therefore be a substantial understatement of the actual increase in allowable losses that would result if the Section 31 limits were removed or significantly increased. For example, about 80 per cent of all part-time farmers with losses report losses under $5,000 and could potentially create larger losses to benefit from an increase in the limit."

In attempting to become established in farming, a combined income farmer may rely on the wages of an off-farm job to meet personal living expenses. Any surplus off-farm funds he may have for investment

in his farm will in many cases already have been taxed. There is no incentive for him to pay operating costs from personal income or borrow money to invest in the farm if the additional cost of interest cannot be claimed as an expense when total losses exceed $5,000. Self-restraint is enforced by the legislation and not by the lack of desire to become better established in farming.

Surely the intent to become better established in farming must be a criteria in measuring eligibility for deduction of losses from total income.

We do not propose that Section 31 be eliminated from the Act but rather that the intent of an individual to become established in farming be given greater priority in establishing status and eligibility for deductibility of farm losses from total income.

The combined income farmer might apply for full loss exemption status and be profiled to establish intent with respect to such matters as:

i) Current occupation or profession and the length of time so occupied;

ii) Background in farming;

iii) The reasons for seeking off-farm income and the amount of off-farm income directly invested into the operation;

iv) The amount of outstanding loans related to the operation;

v) The amount of personal time devoted to the farming operation itself;

vi) Place of residency or family residency;

vii) The future expectation of profit from the operation.

We submit that a combined income farmer who successfuly applies

for full exemption status of farm losses should be placed in an eligible classification by Revenue Canada if able to satisfy the criteria. He should then be permitted to develop his farming plans without the continuing threat of harassment of the tax inspector. The classification status could be reviewed periodically, such as every 5 years, to assess progress toward sufficiency, and renewed for a further period. Persons especially engaged by Revenue Canada could be utilized for that purpose.

Our organization supports as well the continuation of cash accounting as the most practical means of calculating annual farm tax returns. We believe it would be impractical to impose on accrual system of taxation on farmers. This is particularly so in circumstances of unstable farm product prices or depressed sales opportunities.

We hold no brief for persons who clearly have no real priority in becoming farmers and are using land only as a speculative commodity. Such individuals should have no tax breaks on farming losses and be subjected to full capital gain taxes when they sell off their holdings.

The elimination of this class of operator from the part-time farming category would ease the pressure on land prices and put the social purpose for which land is intended into a more acceptable perspective.

CONCLUSION:

This Committee has undertaken the study of three specific areas of concern to farmers.

The high cost of interest charges burdening many in farming may be corrected in ways other than by direct subsidy or agribonds as outlined in this submission. The essential consideration is that something concrete and constructive be done soon to redirect the course of the farm finance crisis.

The matter of capital gains is comparatively straight-forward.

Farmers who have devoted perhaps a lifetime to the production of food and often received less than real production costs in return need to be treated fairly upon the liquidation of their assets in order that their retirement years can be spent in dignity.

Obstacles attendant with Section 31 preventing part-time farmers who genuinely are attempting to become established in farming must be removed. Conversely, farm land investment and losses should not be permitted to serve as a tax dodge haven for those who are seeking to circumvent their responsibility to society.

In short, we remind the Committee that in these matters justice needs not only appear to be done but must indeed be done.

- 30 -

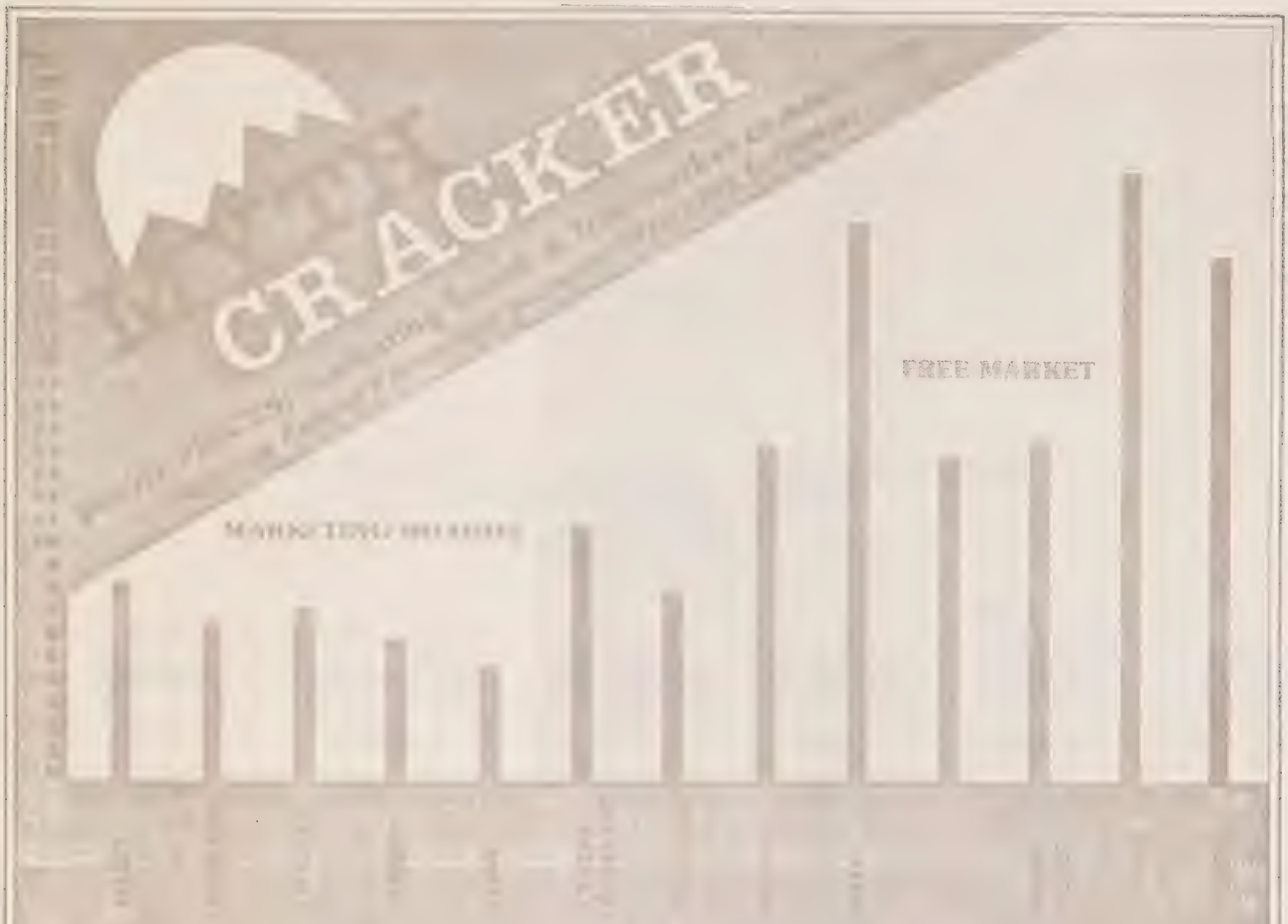
All of Which is Respectfully
Submitted by:

NATIONAL FARMERS UNION

APPENDIX A

APPENDIX B

APPENDIX A



MYTH...

CRACKER

All prices have increased. Food prices are no exception. Between 1961 and 1980, food prices increased [illegible] average of 12.1%. Yet wages kept up. Canadians were spending almost 5% less of their disposable income on food in 1980, than they were in 1961. Higher food prices, at a declining cost to consumers.

The time has come for a little reason. The time has come to look rationally at the egg myths.

APPENDIX B

Farm Cash Receipts, Operating & Depreciation Charges
Realized Net Income - Canada
1975 - 1984

($ Billions)

Year	Cash Receipts	Operating & Depreciation	Realized Net Income	O & D as % of C.R.	Farm Input Index (1971=100)	R.N.I. in Constant $
1975	10.1	6.6	3.8	65.3	162.4	3.8
1976	10.1	7.3	2.9	72.3	172.8	2.7
1977	10.2	7.8	2.6	76.5	180.0	2.3
1978	12.0	9.1	3.1	75.8	201.1	2.5
1979	14.3	11.0	3.5	76.9	234.9	2.4
1980	15.8	12.7	3.4	80.4	257.6	2.1
1981	18.5	14.8	4.2	80.0	294.4	2.3
1982	18.8	15.6	3.5	83.0	303.3	1.9
1983	18.7	15.7	3.3	84.0	307.1	1.7
1984*	20.0	16.4	3.8	82.0	318.9	1.9

* Preliminary

Source - Statistics Canada